Life Insurance as an Asset Class: A Predictable Asset for Unpredictable Times

Producer Guide

This material is not intended to be used to avoid tax penalties. It was prepared to support the promotion or marketing of the matter addressed in this document. Clients should be advised to seek advice from an independent tax advisor.

LIFE

ING

Your future. Made easier.®

A Predictable Asset for Unpredictable Times

Clients who have more money than they will spend will pass the excess on to others at death. Efficiently passing on assets left at death can be challenging, especially when the future value of assets and the state of the markets for them are relatively unpredictable. To maximize the part of their estates they intend to transfer to family members, clients should review the assets that make up that part of their estates and ask if life insurance might help them achieve a better result.

What Features Make Wealth Transfer Easier?

When it comes to transferring wealth at death, not all assets are created equal. Different assets are subject to different risks, different taxes rates and different management costs. Some assets produce better results for wealth transfer than others. Clients who want their estate plans to transfer their wealth with the most financial efficiency need to look at their assets from a wealth transfer perspective. Assets that are effective in transferring wealth to surviving family members may have features like these:

- Value at death is known in advance with relative certainty
- Value at death isn't impacted by changes in the stock market or interest rates
- Easily convertible into cash without additional costs or taxes
- Likely to grow in value
- Growth in the asset's value is income tax free
- Can be positioned so that estate taxes are not increased
- Can be passed on without the delays and expenses of probate.

Many clients may have financial products from banking, investment or insurance companies in their estates. In addition to the features listed above, wealth transfer planning can be more efficient when each company providing the financial product:

- Has made some guarantees about product performance
- Is financially strong enough to keep its promises concerning the product
- Is subject to meaningful government regulation and oversight
- Has its financial strength independently reviewed by outside rating agencies who publish their findings.

How Does Life Insurance Measure Up?

Life insurance is one of the few financial products that has a combination of these potential advantages:

1. **Predictable Value** – The policy may be structured to pay a known death benefit amount when the insured dies.
2. **Value Not Directly Linked to Market Performance** – The policy may be structured so that the death benefit may not directly depend on financial market performance.
3. **Liquidity** – The death benefits are automatically paid in cash; generally no income taxes, transfer costs, commissions or management fees are subtracted from the death benefit.
4. **Growth/Leverage** – Premiums paid for death benefit protection can provide significant leverage in the early years and may provide a competitive rate of return through life expectancy.
5. **Income Tax-Free Payment** – Policy death benefits (including the amount in excess of premiums paid) are generally income tax free under IRC Section 101.
6. **Easily Divisible** – Death benefits can be easily divided among several beneficiaries; through the beneficiary designation the policy owner directs how the proceeds should be distributed.
7. **Avoids Probate** – Death benefits may be structured to be paid directly to the beneficiaries without the costs and delays that often impact assets distributed through the probate court system.
8. **May Avoid Estate Taxes** – Ownership of the policy may be structured so that the death benefits will not be subject to federal estate taxes as part of the insured's taxable estate.
9. **Subject to Government Oversight** – All life insurance policies offered for sale as well as the insurance companies and representatives who sell them must satisfy state standards.

What Are the Risks with Life Insurance?

No wealth transfer strategy or financial product is appropriate for every person every time. There are always risks. Wise people stop to evaluate those risks before deciding to purchase the product. These are some of the potential risks that clients should consider before using life insurance in their wealth transfer plan:

Is coverage available at a reasonable rate? Not everyone can purchase life insurance coverage. Insurers only issue policies to people who are in reasonably good health and who can show they need the coverage. People who are in poor health must pay higher premiums (assuming the insurer will offer them a policy at all).

Will the policy owner pay the premiums as required? Once the amount of coverage and premium amount are established, the policy owner must pay the premiums in order for the policy to stay in force. If the premiums are not paid in a timely manner, the policy may be terminated and the coverage lost.

Will the life insurance company be able to pay the death benefit? Once a policy is purchased, the owner is relying on the insurance company to stay in business so it can keep its promise to pay the death benefit when the insured dies. Fortunately, independent rating agencies regularly review the financial condition of most life insurance companies and rate them publicly on their financial strength. This information can help clients decide if they want to move their coverage to a stronger insurance company.

How long will the insured live? Since policy death benefits aren't payable until the insured's death, it may be some time before the beneficiary receives any money. Thus, the longer the insured lives, the lower the rate of return on premiums paid into the policy.

Does Life Insurance Make Financial Sense?

No matter how many features a financial product has, it should only be used when it makes financial sense. Life insurance is designed to provide a cash payment at death that may be used in a variety of ways to accomplish clients' wealth transfer goals.

Rate of Return Analysis

This technique focuses on the estimated internal rate of return (IRR) the policy death benefit is expected to achieve each year relative to the premiums paid in. It is impossible to determine the exact rate of return the policy will deliver until the insured dies and the death benefits are paid. Nevertheless, a rate of return can be reasonably determined each year by comparing the likely death benefit with the total premiums paid. Internal rates of return can be made for a series of years. The insurance company's product illustration system may be able to calculate and print annual internal rates of return.

Life insurance policy internal rates of return are generally high during the early years of coverage. That's because the death benefit payable can be quite large in relation to the premiums paid. Each year the policy is in force the internal rate of return is reduced. This series of internal rates of return can be analyzed. The rates of return for the years close to the insured's life expectancy should probably receive the most scrutiny. If the client feels they are in an acceptable range at probable life expectancy, then it may make financial sense to use life insurance for wealth transfer. If they are unacceptable, other uses for the premium dollars should be considered.

Comparison to a Different Asset

Another way to evaluate the financial efficiency of a life insurance policy is to compare its projected performance to that of a different asset (e.g. a stock or mutual fund). A financial model can be created to make the comparison. Such a model would require many assumptions (which may or may not come true). As long as the assumptions used are reasonable, the results may provide valuable information and a frame of reference for deciding if life insurance should be used as one of the components of an integrated wealth transfer strategy.

The Life Insurance as an Asset Class (LIAAC) Illustration in ING Presents

The ING Presents software illustration system gives users the opportunity to produce a customized LIAAC illustration for the policy they wish to illustrate. The LIAAC illustration capability is NOT available for VUL policies from ING member companies. On non-VUL policies ING Presents users may compute and/or print any or all of four optional reports:

1. IRR Report
2. Comparison to a Different Asset Report
3. Retained Capital Report – This report computes the relative cash flows and other financial ramifications of funding the life insurance policy in two different premium scenarios.
4. Gifting with Life Insurance Report (see section below).

Gifting With Life Insurance

To preserve the value of the net worth they've built, it may make sense for wealthy clients to give away some assets before death. If they are in good health, their tax and legal advisors may recommend using life insurance as part of their lifetime gifting strategy. In addition to the potential advantages of life insurance summarized on page 2 of this Guide, there are some additional potential factors that can make life insurance a valuable transfer tool for the wealthy:

1. Wealthy people usually don't personally own the life insurance policies that insure their lives. To avoid estate and generation skipping taxes, their policies are often owned by younger family members or by trusts for their benefit. In these cases, they don't need to give away the policy. Instead, they only need to provide the funds the policy owner needs to pay the premiums.
2. Unlike most assets, life insurance policies are rarely paid for in one lump sum. Policy premiums are usually paid in a series of annual installments. Gifts of cash to pay premiums can be structured so they are gift tax free under tax exemptions established by Congress and the IRS (e.g. $13,000 in 2009 per donee for annual exclusion gifts; non-present interest gifts may total up to $1,000,000 over a donor's lifetime). With careful planning, cash can be transferred to pay premiums without triggering gift taxes.
3. Gifts of cash for premiums can do "double duty" in reducing the insured's federal estate taxes. First, gifts of premiums reduce the size of the taxable estate. Second, when the insured doesn't own the policy, the death benefits may be excluded from the taxable estate. As a result, more money may stay in the family.

For some people, this combination of potential advantages is important, but not enough. They want proof that life insurance will provide good value for the premiums paid in. They may be interested in a numerical analysis that evaluates a particular policy's financial efficiency. They may find an internal rate of return (IRR) analysis helpful. They may also wish to see a comparison of life insurance with a different financial asset.

The Comparison to a Different Asset report in the LIAAC illustration in ING Presents may be persuasive in demonstrating that gifting through a life insurance policy's death benefit may be a useful and efficient way to preserve and transfer family wealth. If the projected life insurance death benefit is greater than the projected after tax value of an alternative investment past the insured's life expectancy, then a case may be made for using life insurance.

Potential Uses for Life Insurance

Sometimes it may make sense to incorporate life insurance into clients' wealth transfer plans even if the internal rates of return are low or other uses of the premium dollar may generate better cash flows. That's because the income tax free (and potentially estate tax free) life insurance death benefits may help clients' families in ways other assets can't. Life insurance death benefits can be used to accomplish a variety of objectives:

- Pay off debts and taxes
- Equalize the inheritances of different family members
- Fund business continuation agreements and succession plans
- Create funds for distribution to charities
- Build funds to educate family members
- Solidify the financial security of disabled family members
- Replace funds lost in troubled financial markets.

Conclusion

Your clients have worked hard to build their net worth. They want to pass the assets that remain at death efficiently and with as little waste as possible. Together with their tax and legal advisors, you can help them consider the taxes, costs and problems individual assets may trigger during the transfer process; and assist them by suggesting strategies to minimize potential losses. Life insurance may be able to help. Using life insurance as a component of their plan may increase the portion of their net worth they are able to pass on to their family. A well-structured life insurance policy may help them accomplish many of their wealth transfer goals.

Want to hear more? Call your ING Life Companies' Representative or ING Life Sales Support at 866-ING-SELL (866-464-7355).

ReliaStar Life Insurance Company
20 Washington Avenue South
Minneapolis, MN 55401

ReliaStar Life Insurance Company of New York
1000 Woodbury Road, Suite 208
Woodbury, NY 11797

Security Life of Denver Insurance Company
1290 Broadway
Denver, CO 80203

Log in to ING for Professionals at www.inglifeinsurace.com

Neither ING nor its affiliated companies or its representatives give tax or legal advice. The strategies suggested may not be suitable for everyone and clients should be advised to consult with their own tax and legal advisors before implementing any of the strategies suggested here.

This material is not intended to be used to avoid tax penalties. It was prepared to support the promotion or marketing of the matter addressed in this document. Clients should be advised to seek advice from an independent tax advisor.

Life insurance products are issued by ReliaStar Life Insurance Company (Minneapolis, MN), ReliaStar Life Insurance Company of New York (Woodbury, NY) and Security Life of Denver Insurance Company (Denver, CO). Within the state of New York, only ReliaStar Life Insurance Company of New York is admitted and its products issued. All are members of the ING family of companies.